DEPARTMENT OF STATE REVENUE

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Letter of Findings Number: 10-0357
Sales and Use Tax
Tax Years: 2007 and 2008

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ISSUE

I. Sales and Use Tax – Public Transportation Exemption.

Authority: IC § 6-8.1-5-1; IC § 6-2.5-2-1; IC § 6-2.5-3-2; IC § 6-2.5-4-1; IC § 6-2.5-5-27; IC § 26-1-2-401; IC § 26-1-2-509; State Dep't of Revenue v. Calcar Quarries, Inc., 394 N.E.2d 939 (Ind. Ct. App. 1979); National Serv-All, Inc. v. Indiana Dep't of State Revenue, 644 N.E.2d 954 (Ind. Tax Ct. 1994); Indiana Waste Systems of Indiana, Inc. v. Indiana Dep't of State Revenue, 644 N.E.2d 960 (Ind. Tax Ct. 1994); Panhandle Eastern Pipeline Co. v. Indiana Dep't of State Revenue, 741 N.E.2d 816 (Ind. Tax Ct. 2001); Carnahan Grain, Inc. v. Indiana Dep't of State Revenue, 828 N.E.2d 465 (Ind. Tax Ct. 2005); Lafayette Square Amoco, Inc. v. Indiana Dep't of State Revenue, 867 N.E.2d 289 (Ind. Tax Ct. 2007); Indiana Dept. of State Rev. v. Kimball Int'l, 520 N.E.2d 454 (Ind. Ct. App. 1988); 45 IAC 2.2-5-61; Black's Law Dictionary 1268 (6th ed. 1991); Sales Tax Information Bulletin 12 (July 2010).

Taxpayer protests the imposition of use tax on transportation equipment purchases.

II. Tax Administration – Ten Percent Negligence Penalty.

Authority: IC § 6-8.1-10-2.1; 45 IAC 15-11-2.

Taxpayer protests the imposition of the negligence penalty.

STATEMENT OF FACTS

Taxpayer is an Indiana corporation that sells farm equipment. Taxpayer often delivered the farm equipment to its customers. The Department conducted a sales and use tax audit of the 2007 and 2008 tax years. The audit determined that Taxpayer had not paid sales tax on certain purchases and had not remitted use tax upon use of the items including vehicles, vehicle repair parts, tires, and fuel purchases, etc. and assessed Taxpayer additional use tax, penalty, and interest. Taxpayer protests the assessment on the basis that the purchase of these items qualified for the public transportation exemption from sales and use tax. A hearing was held on the matter, and this Letter of Findings results.

I. Sales and Use Tax – Public Transportation Exemption.

DISCUSSION

The Department's audit found that Taxpayer purchased items including vehicles, vehicle repair parts, tires, and fuel purchases, etc., for which Taxpayer had not paid sales tax and for which Taxpayer had failed to self-assess use tax. Taxpayer argues that the Department incorrectly assessed use tax because it is entitled to the "public transportation" sales and use tax exemption.

All tax assessments are prima facie evidence that the Department's claim for the unpaid tax is valid; the taxpayer bears the burden of proving that any assessment is incorrect. IC § 6-8.1-5-1(c); Lafayette Square Amoco, Inc. v. Indiana Dep't of State Revenue, 867 N.E.2d 289, 292 (Ind. Tax Ct. 2007).

Pursuant to IC § 6-2.5-2-1, a sales tax, known as state gross retail tax, is imposed on retail transactions made in Indiana unless a valid exemption is applicable. Retail transactions involve the transfer of tangible personal property. IC § 6-2.5-3-2(a). A complementary excise tax, known as the use tax, is imposed on the storage, use, or consumption of tangible personal property in Indiana if the property was acquired in a retail transaction. IC § 6-2.5-3-2.

Specifically, IC § 6-2.5-2-1 provides as follows:

(a) An excise tax, known as the state gross retail tax, is imposed on retail transactions made in Indiana.

(b) The person who acquires property in a retail transaction is liable for the tax on the transaction and, except as otherwise provided in this chapter, shall pay the tax to the retail merchant as a separate added amount to the consideration in the transaction. The retail merchant shall collect the tax as agent for the state.

IC § 6-2.5-3-2(a) provides for the complementary use tax:

An excise tax, known as the use tax, is imposed on the storage, use, or consumption of tangible personal property in Indiana if the property was acquired in a retail transaction, regardless of the location of that transaction or of the retail merchant making that transaction.

The exemption sought is found at IC § 6-2.5-5-27, which states:

Transactions involving tangible personal property and services are exempt from the state gross retail tax, if the person acquiring the property or service directly uses or consumes it in providing public transportation for persons or property.

45 IAC 2.2-5-61 elaborates on the public transportation exemption. The regulation states in relevant part:

(a) The state gross retail tax shall not apply to the sale and storage or use in this state of tangible personal property which is directly used in the rendering of public transportation of persons or property.

(b) Definition: Public Transportation. Public transportation shall mean and include the movement, transportation, or carrying of persons and/or property for consideration by a common carrier, contract carrier, household goods carrier, carriers of exempt commodities, and other specialized carriers performing public transportation service for compensation by highway, rail, air, or water, which carriers operate under authority issued by, or are specifically exempt by statute or regulation from economic regulation of, the public service commission of Indiana, the Interstate Commerce Commission, the aeronautics commission of Indiana, the U.S. Civil Aeronautics Board, the U.S. Department of Transportation, or the Federal Maritime Commissioner; however, the fact that a company possesses a permit or authority issued by the P.S.C.I., I.C.C., etc., does not of itself mean that such a company is engaged in public transportation unless it is in fact engaged in the transportation of persons or property for consideration as defined above.

(c) In order to qualify for exemption, the tangible personal property must be reasonably necessary to the rendering of public transportation. The tangible personal property must be indispensable and essential in directly transporting persons or property.

Indiana courts have interpreted the public transportation exemption in a series of cases including State Dep't of Revenue v. Calcar Quarries, Inc., 394 N.E.2d 939 (Ind. Ct. App. 1979) (holding that the tangible personal property being transported must be the property of another); National Serv-All, Inc. v. Indiana Dep't of State Revenue, 644 N.E.2d 954 (Ind. Tax Ct. 1994) (holding that to be entitled to the public transportation exemption, a carrier must transport tangible personal property of another and for consideration); Indiana Waste Systems of Indiana, Inc. v. Indiana Dep't of State Revenue, 644 N.E.2d 960 (Ind. Tax Ct. 1994) (holding that a taxpayer must use the tangible personal property predominately in public transportation in order to qualify for the exemption); Panhandle Eastern Pipeline Co. v. Indiana Dep't of State Revenue, 741 N.E.2d 816 (Ind. Tax Ct. 2001) (holding that the public transportation predominant use exemption is an all or nothing exemption); Carnahan Grain, Inc. v. Indiana Dep't of State Revenue, 828 N.E.2d 465 (Ind. Tax Ct. 2005) (holding that it is the predominant use of the property that determines whether a taxpayer involved in multiple lines of business is entitled to the public transportation exemption, and not whether a taxpayer, as an overall business, is predominately engaged in public transportation).

In summary, in order to qualify for the public transportation exemption, Taxpayer must show that the equipment purchased was predominantly used to transport the property of another for which the Taxpayer received consideration. Further clarification is found in Sales Tax Information Bulletin 12 (July 2010), which states that "tangible personal property is predominately used in public transportation if more than 50 [percent] of its use is attributable to transporting people or property for hire."

In applying any tax exemption, the general rule is that "tax exemptions are strictly construed in favor of taxation and against the exemption." Indiana Dept. of State Rev. v. Kimball Int'l Inc., 520 N.E.2d 454, 456 (Ind. Ct. App. 1988).

Taxpayer purchased two vehicles during the audit period, a Peterbilt semi tractor and a Ford pickup truck. The audit found that when the Peterbilt was used to deliver farm equipment to its customers after their customers purchased the equipment, ownership of the equipment was transferred to the customer upon delivery, and therefore the transportation of the equipment was not public transportation.

Taxpayer disagreed with this conclusion. Taxpayer claims that ownership transferred when the contract was signed. Taxpayer points to a clause in the signature portion of its "Retail Installment Sale Contract and Security Agreement" (Agreement) to substantiate its claim that title passed to the purchaser prior to delivery. The Agreement provides that "I have received and examined the Equipment," which Taxpayer asserts should be interpreted to mean that their customers have effectively taken possession of the equipment at that point. Taxpayer goes on to state that the contract is signed at Taxpayer's place of business, and that payment is made prior to delivery. The transportation of the equipment was listed as a separate expense on the sales invoices.

However, IC § 6-2.5-4-1 provides that:

(a) A person is a retail merchant making a retail transaction when he engages in selling at retail.

(b) A person is engaged in selling at retail when, in the ordinary course of his regularly conducted trade or business, he:

(1) acquires tangible personal property for the purpose of resale; and

(2) transfers that property to another person for consideration.

(c) For purposes of determining what constitutes selling at retail, it does not matter whether:

(1) the property is transferred in the same form as when it was acquired;

(2) the property is transferred alone or in conjunction with other property or services; or

(3) the property is transferred conditionally or otherwise.

...

(e) The gross retail income received from selling at retail is only taxable under this article to the extent that the income represents:

(1) the price of the property transferred, without the rendition of any service; and

(2) except as provided in subsection (g), any bona fide charges which are made for preparation, fabrication, alteration, modification, finishing, completion, delivery, or other service performed in respect to the property transferred before its transfer and which are separately stated on the transferor's records.

For purposes of this subsection, a transfer is considered to have occurred after delivery of the property to the purchaser.

(Emphasis added).

According to IC § 6-2.5-4-1, the sales of equipment were not complete until the equipment was delivered to Taxpayer's customers. Further, the Department also notes that in the Uniform Commercial Code as codified by the Indiana General Assembly, IC § 26-1-2-401(2) instructs:

Unless otherwise explicitly agreed, title passes to the buyer at the time and place at which the seller completes his performance with reference to the physical delivery of the goods...

IC § 26-1-2-509 goes on to state that:

(1) Where the contract requires or authorizes the seller to ship the goods by carrier:

(a) if it does not require him to deliver them at a particular destination, the risk of loss passes to the buyer when the goods are duly delivered to the carrier even though the shipment is under reservation (IC 26-1-2-505); but

(b) if it does require him to deliver them at a particular destination and the goods are there duly tendered while in the possession of the carrier, the risk of loss passes to the buyer when the goods are there duly so tendered as to enable the buyer to take delivery.

(2) Where the goods are held by a bailee to be delivered without being moved, the risk of loss passes to the buyer:

(a) on his receipt of possession or control of a negotiable document of title covering the goods; or

(b) on acknowledgment by the bailee of the buyer's right to possession of the goods; or

(c) after his receipt of possession or control of a nonnegotiable document of title or other direction to deliver in a record, as provided in IC 26-1-2-503(4)(b).

(3) In any case not within subsection (1) or (2), the risk of loss passes to the buyer on his receipt of the goods if the seller is a merchant. Otherwise the risk passes to the buyer on tender of delivery.

(Emphasis added).

Furthermore, Black's Law Dictionary defines "receive" as "to take into possession and control; accept custody of; collect." Black's Law Dictionary 1268 (6th ed. 1991).

Regardless of when the Agreement was signed or when payment was made, the Agreement states nothing about delivery of the equipment or risk of loss. Pursuant to IC § 26-1-2-401(2), transfer of title did not occur until the product was delivered to its buyers' locations. Likewise, despite what is stated in the Agreement, the equipment was not "received" until it was delivered to its buyers' locations because the buyers did not take "possession and control" or "accept custody" of the equipment until that time. As Taxpayer still held title to and possessed the equipment being delivered, Taxpayer was not transporting the property of another. Taxpayer, therefore, was not providing "public transportation" services in these instances. A majority of the remaining mileage was accumulated when the Peterbilt was being used for only the Taxpayer's benefit. Since the Peterbilt was not predominately used to transport the property of another, Taxpayer has not met its burden of proof to establish that the purchase of the Peterbilt and associated repair parts, tires, and fuel purchases, were exempt from sales tax.

As for the Ford, Taxpayer claims that it was used to pick up and deliver equipment for its customers in order to repair the equipment at its service shop. Taxpayer provided a mileage breakdown, showing miles that the Ford accumulated when it transported its customers' equipment, and miles that the Ford accumulated when it was being used for only the Taxpayer's benefit. According to this breakdown, approximately 33.8 percent of the mileage was accumulated when transporting its customers' equipment. Since the Ford was not predominantly used to transport the property of another, Taxpayer has not met its burden of proof to establish that the purchase of the Ford and associated repair parts, tires, and fuel purchases, were exempt from sales tax.

FINDING

Taxpayer's protest is respectfully denied.

II. Tax Administration – Ten Percent Negligence Penalty.

DISCUSSION

The Department issued proposed assessments and the ten percent negligence penalty and interest for the tax years in question. Taxpayer protests the imposition of penalty, requesting that it be waived.

Taxpayer protests the imposition of the ten percent negligence penalty pursuant to IC § 6-8.1-10-2.1. Indiana Regulation 45 IAC 15-11-2(b) clarifies the standard for the imposition of the negligence penalty as follows:

Negligence, on behalf of a taxpayer is defined as the failure to use such reasonable care, caution, or diligence as would be expected of an ordinary reasonable taxpayer. Negligence would result from a taxpayer's carelessness, thoughtlessness, disregard or inattention to duties placed upon the taxpayer by the Indiana Code or department regulations. Ignorance of the listed tax laws, rules and/or regulations is treated as negligence. Further, failure to read and follow instructions provided by the department is treated as negligence. Negligence shall be determined on a case by case basis according to the facts and circumstances of each taxpayer.

45 IAC 15-11-2(c) provides that:

The department shall waive the negligence penalty imposed under IC 6-8.1-10-1 if the taxpayer affirmatively establishes that the failure to file a return, pay the full amount of tax due, timely remit tax held in trust, or pay a deficiency was due to reasonable cause and not due to negligence. In order to establish reasonable cause, the taxpayer must demonstrate that it exercised ordinary business care and prudence in carrying out or failing to carry out a duty giving rise to the penalty imposed under this section. Factors which may be considered in determining reasonable cause include, but are not limited to:

(1) the nature of the tax involved;
(2) judicial precedents set by Indiana courts;
(3) judicial precedents established in jurisdictions outside Indiana;
(4) published department instructions, information bulletins, letters of findings, rulings, letters of advice, etc;
(5) previous audits or letters of findings concerning the issue and taxpayer involved in the penalty assessment.

Reasonable cause is a fact sensitive question and thus will be dealt with according to the particular facts and circumstances of each case.

In this case, Taxpayer incurred a deficiency which the Department determined was due to negligence under 45 IAC 15-11-2(b), and so was subject to a penalty under IC § 6-8.1-10-2.1(a).

Taxpayer has not sufficiently established that its failure to pay the sales tax was due to reasonable cause and not due to negligence, as required by 45 IAC 15-11-2(c).

FINDING

Taxpayer's protest is respectfully denied.

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